98TH CONGRESS
2d Session

SENATE

REPORT
98-575

RETIREMENT EQUITY ACT OF 1984

AUGUST 6, 1984.—Ordered to be printed

Mr. DOLE, from the Committee on Finance, submitted the following

REPORT

[To accompany H.R. 4280]

[Including cost estimate of the Congressional Budget Office]

The Committee on Finance, to which was referred the bill (H.R. 4280) to amend the Employee Retirement Income Security Act of 1974 and the Internal Revenue Code of 1954 to improve the delivery of retirement benefits and provide for greater equity under private pension plans for workers and their spouses and dependents by taking into account changes in work patterns, the status of marriage as an economic partnership, and the substantial contribution to that partnership of spouses who work both in and outside the home, and for other purposes, having considered the same, reports favorably thereon with an amendment and recommends that the bill as amended do pass.

37-050 O

I. SUMMARY

1. Periods of Employee Service Taken Into Account Under Pension, Profit-Sharing, and Stock Bonus Plans

Maximum age conditions.—The bill reduces from 25 to 21 the maximum age a pension, profit-sharing, or stock bonus plan (pension plan) generally can require an employee to attain as a condition of becoming a participant in the plan. Additionally, a plan is not permitted to ignore service after age 18 for purposes of determining the vested portion of a participant's benefit. The bill also makes changes to the maximum age conditions for employees of certain educational institutions.

Break in service rules.—The bill provides that, in the case of a nonvested participant, years of service with the employer or employers maintaining a pension plan before any period of consecutive 1-year breaks in service are required to be taken into account for participation and vesting purposes after a break in service unless the number of consecutive 1-year breaks in service equals or exceeds the greater of (1) 5 years or (2) the aggregate number of years of service before the consecutive breaks in service.

In addition, the bill provides that, in the case of a participant in certain plans, years of service after a break in service must be counted for purposes of determining the vested percentage of the participant's accrued benefit derived from employer contributions before the break in service unless the participant incurs at least 5 consecutive 1-year breaks in service.

Maternity and paternity leave.—The bill provides rules relating to crediting of service for cases in which an employee is absent from work because of maternity or paternity leave. Under the bill, certain hours of absence (up to 501 hours) on account of pregnancy, birth, adoption, or certain child care are taken into account in determining whether a break in service has occurred under the participation and vesting rules.

2. Survivor Benefit Requirements

Under the bill, a defined benefit or money purchase pension plan is required to provide automatic survivor benefits (1) in the case of a participant who retires under the plan, in the form of a qualified joint and survivor annuity, and (2) in the case of a vested participant who dies before the annuity starting date and who has a surviving spouse, in the form of a qualified preretirement survivor annuity. An exception is provided under the bill for a money purchase pension plan that is adopted as part of an employee stock ownership plan (ESOP). The automatic survivor benefit also applies to any participant under a profit-sharing or stock bonus plan unless (1) the participant does not elect benefits in the form of a life annuity, (2) the plan pays the full vested account balance to the

participant's surviving spouse if the participant dies, and (3) the plan is not a direct or indirect transferee of a plan required to provide automatic survivor benefits.

Under the bill, a participant is to be given the opportunity to waive the qualified joint and survivor annuity and the qualified preretirement survivor annuity unless the plan fully subsidizes the cost of those benefits. In addition, an election to waive a qualified joint and survivor annuity or a qualified preretirement survivor annuity is not to be effective unless it is in writing and is signed by the participant and the participant's spouse.

The bill generally defines the period during which a participant may waive a survivor benefit (or revoke such a waiver) to mean (1) in the case of a qualified joint and survivor annuity, a period of time not to exceed 90 days before the annuity starting date; or (2) in the case of a qualified preretirement survivor annuity, a period beginning on the first day of the plan year in which the participant attains age 35 and ending on the date of the participant's death.

3. *Assignment or Alienation of Benefits in Divorce, Etc., Proceedings*

In the case of a judgment, decree, or order relating to child support, alimony payments, or marital property rights pursuant to a State domestic relations law that meets certain requirements (a qualified domestic relations order), the bill clarifies that such order does not result in a prohibited assignment or alienation of benefits under the spendthrift provisions of the Code or ERISA. In addition, the bill provides that the general ERISA preemption rule does not apply to these qualified domestic relations orders.

The bill requires that a qualified domestic relations order identify the parties involved and provide specific instructions for determining the portion of plan benefits payable to an alternate payee (a spouse, former spouse, child, or other dependent) under the order. The bill requires that benefits under the order be in a form otherwise provided by the plan. The bill provides procedures to be followed by the plan administrator when the benefits payable under an order are in dispute.

4. *Cash Out of Certain Accrued Benefits*

Under the bill, a plan is treated as providing nonforfeitable benefits even if the plan provides for a cash out of a separated participant's benefit without the participant's consent if the present value of the benefit does not exceed $3,500. The limit under present law is $1,750. For purposes of determining the present value of the participant's benefit, the bill provides that a plan may not use an interest rate that is greater than the rate used by the Pension Benefit Guaranty Corporation (PBGC) for valuing a lump sum distribution upon plan termination.

5. *Notice of Forfeitability of Benefits*

Present law requires that a plan furnish a participant with a statement of benefits under certain circumstances. The bill requires that the statement include a notice that certain benefits may be forfeitable in the event the participant dies before a particular date.

6. Notice of Rollover Treatment

Under present law, a plan administrator is not required to notify a plan participant receiving a qualifying rollover distribution that the distribution may be rolled over, tax-free, within 60 days after the date of the distribution. The bill requires the plan administrator to provide notice to participants and beneficiaries that distributions may be eligible for (1) rollover to an IRA or another qualified plan or (2) 10-year income averaging. The Secretary of the Treasury is to develop officially approved notices that may be used to satisfy this requirement.

7. Reduction of Accrued Benefits

Under present law, a pension plan must provide definitely determinable benefits. A pension plan may not be amended to reduce previously accrued benefits. The bill includes provisions relating to the permitted effect of plan amendments with respect to previously accrued benefits.

8. Study by the General Accounting Office

The bill directs the General Accounting Office (GAO) to conduct a detailed study of the effect on women of the rules relating to pension, profit-sharing, and stock bonus plans. The results of this study are to be reported to various committees of the Congress no later than January 1, 1990.

9. Effective Dates

The provisions of the bill generally are effective for plan years beginning after December 31, 1984. In the case of a plan maintained pursuant to one or more collective bargaining agreements ratified by the date of enactment between employee representatives and one or more employers, the provisions are generally not effective for plan years beginning before the earlier of (1) the date on which the last of the collective bargaining agreements relating to the plan terminates (determined without regard to any extension agreed to after the date of enactment) or (2) January 1, 1987. Special effective dates apply with respect to the qualified survivor benefit provisions and with respect to reductions of accrued benefits.

II. EXPLANATION OF THE BILL

A. Periods of Employee Service Taken Into Account Under Pension, Profit-Sharing, and Stock Bonus Plans (Secs. 102 and 202 of the bill, secs. 202 and 203 of ERISA, and secs. 410 and 411 of the Code)

Present Law

Minimum participation, vesting, and benefit accrual requirements

In general

If a pension, profit-sharing, or stock bonus plan qualifies under the tax law ("qualified plan"),[1] then (1) a trust under the plan generally is exempt from income tax, (2) employers generally are allowed deductions (within limits) for plan contributions for the year for which the contributions are made even though participants are not taxed on plan benefits until the benefits are distributed, (3) benefits distributed as a lump sum distribution are accorded special long-term capital gain or 10-year income averaging treatment, or may be rolled over, tax-free, to an individual retirement account (IRA) or to another qualified plan, and (4) limited estate and gift tax exclusions may be available.

Under a pension, profit-sharing, or stock bonus plan ("pension plan"), benefits are provided to participants under plan formulas that determine the amount of the benefit a participant may earn, the portion of that benefit that has been earned, and the portion of the earned benefit that is vested or nonforfeitable. Accordingly, plans provide rules for determining whether an employee is a plan participant (the employee participation rules), for measuring benefits (the benefit formula), for determining the portion of the benefit that has been earned (the benefit accrual rules), and for determining the vested percentage of a participant's accrued benefit (the vesting schedule). If a joint and survivor benefit is not provided and the participant dies before payment of benefits commences, the participant's surviving spouse may not be eligible to receive benefits under the plan.

Under present law, a pension plan must satisfy certain minimum standards relating to the conditions under which employees may be excluded from plan participation, to the method under which plan benefits are accrued, and to the vesting schedule. The participation standards limit the permissible exclusions based on the age and period of service completed by an employee.[2] The benefit accrual

[1] Sec. 401(a) or 403(a) of the Code.

[2] In addition, the Code provides minimum coverage rules for qualified pension plans. These rules are designed to require that qualified pension plans provide participation to a minimum percentage of employees or to a broad cross-section of employees.

standards are based upon the number of years of plan participation. The vesting schedule standards are generally based upon the number of years of service with the employer that the employee has completed.

Participation

Under present law,[3] a pension plan generally may not require an employee to complete more than one year of service or attain an age greater than 25 as a condition of plan participation.[4] Employees of certain educational institutions may be excluded from plan participation up to age 30 under present law.

For purposes of the participation requirements, the term "year of service" generally means a consecutive 12-month period during which an employee has worked at least 1,000 hours.[5] The first 12-month period is measured from the date the employee begins service with the employer (or, under certain circumstances, a predecessor employer). Accordingly, an employee has fulfilled the year of service requirement if at least 1,000 hours of service are completed by the first anniversary date of employment. Later 12-month periods may be based on the plan year.

Vesting

The rules for pension plans generally require that a plan meet one of three alternative minimum vesting schedules.[6] Under these schedules, an employee's right to accrued benefits derived from employer contributions become nonforfeitable (vest) to varying degrees upon completion of specified periods of service with an employer (or, under certain circumstances, a predecessor employer). An employee's right to benefits derived from employee contributions is immediately nonforfeitable.

Under one of the minimum schedules, full vesting is required upon completion of 10 years of service (no vesting is required before the end of the 10th year).[7] Under a second schedule, vesting begins at 25 percent after completion of 5 years of service and increases gradually to 100 percent after completion of 15 years of service.[8] Under these two vesting schedules, all years of service with the employer maintaining the plan after attainment of age 22 generally must be taken into account for purposes of determining an employee's vested percentage. The third schedule takes both age and service into account, but in any event requires 50 percent vesting after 10 years of service and an additional 10 percent vesting for each year thereafter until 100 percent vesting is attained after 15 years of service.[9] Under this schedule, all years of service with

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[3] Sec. 410(a) of the Code.

[4] Accordingly, an employee generally may not be excluded from plan participation on the basis of length of service if the employee has completed one year of service and generally may not be excluded on the basis of age if the employee has attained age 25. An employee who has completed one year of service and who has attained age 25 may, however, be excluded from plan participation on other grounds (for example, a plan may be limited to employees within a particular job classification).

[5] Sec. 410(a)(3) of the Code.

[6] Sec. 411(a) of the Code.

[7] Sec. 411(a)(2)(A) of the Code.

[8] Sec. 411(a)(2)(B) of the Code.

[9] Sec. 411(a)(2)(C) of the Code.

the employer (including years of service prior to age 22) must be taken into account for purposes of determining an employee's vested percentage if, during those years, the employee participated in the plan. A faster vesting schedule is required if the employer maintains a qualified plan that is a top-heavy plan.[10]

Under present law, certain forfeitures of vested benefits are permitted. Thus, a right to an accrued benefit derived from employer contributions is not treated as forfeitable merely because the plan does not pay benefits after the participant dies (other than the payment of a survivor benefit required under the qualified joint and survivor annuity rules).

Break in service rules

In general, all years of service with the employer maintaining a pension plan are taken into account for purposes of the minimum participation requirements. No credit need be provided, however, for periods during which an employee is considered to have a break in service. In some cases, an employee who returns to work for an employer after a break in service may lose credit for pre-break service.

A plan may provide that a 1-year break in service occurs in a 12-month measuring period in which the employee does not complete more than 500 hours of service.[11] If an employee has incurred a 1-year break in service, the plan may require a 1-year waiting period before reentry. Upon reentry, the employee's pre-break and post-break service generally are required to be aggregated, and the employee is required to receive full credit for the reentry waiting period service if any part of the employee's benefit derived from employer contributions was vested or if the number of 1-year breaks in service is less than the number of years of service completed before the break (the "rule of parity").[12] A plan may provide that an employee who completes more than 500 hours of service but fewer than 1,000 hours of service has neither a 1-year break in service nor a year of service for participation purposes.

Break in service rules also apply under the vesting rules. The break in service rules applicable in determining the number of years of service taken into account for vesting purposes under a defined benefit plan[13] are similar to the break in service rules that apply for plan participation purposes. A special break in service rule applies for purposes of the vesting rules in the case of a defined contribution plan.[14] Post-break service need not be taken into account under such a plan in determining the nonforfeitable percentage for employer contributions made before the break in service.[15]

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[10] Also, faster vesting may be required to prevent discrimination in favor of employees who are officers, owners, or highly compensated.

[11] Sec. 410(a)(5) of the Code.

[12] Sec. 410(a)(5) of the Code.

[13] Other than certain defined benefit plans funded solely with insurance contracts.

[14] This special rule also applies to certain defined benefit plans funded solely with insurance contracts.

[15] Sec. 411(a)(6)(C) of the Code.

Benefit accruals

Present law [16] requires that a participant in a defined benefit pension plan accrue (earn) the normal retirement benefit provided by the plan at certain minimum rates. The accrual rules are designed to limit backloading of benefit accruals as a technique to avoid the minimum vesting standards. Under a backloaded accrual schedule, a larger portion of the benefit is earned each year in later years of service. Accordingly, under a plan with backloaded accruals, an employee who separates from service before reaching retirement age earns a disproportionately lower share of the benefit.

Maternity or paternity leave

For purposes of the minimum participation, vesting, and benefit accrual requirements, a pension plan is not required to give an employee credit for periods of time during which the employee is not compensated for maternity or paternity leave. A pension plan generally is required to credit sufficient hours, up to 501 hours of service for participation and vesting purposes, for paid maternity or paternity leave in order to prevent a break in service.

Reasons for Change

The committee recognizes that the rules of present law relating to the maximum age conditions and years of service counted for vesting service tend to disadvantage women workers. In addition, the present law break in service rules often make it difficult for an individual to take an adequate leave of absence from work on account of the birth or adoption of a child without loss of credit for participation and vesting purposes under the employer's qualified plan.

Explanation of Provisions

Maximum age conditions

The bill provides that a pension plan may not require, as a condition of participation, completion of more than one year of service or attainment of an age greater than 21 (whichever occurs later).[17] The reduction in the maximum participation age further limits the extent of backloading of benefit accruals.

Under the bill, a plan is not permitted to ignore, for purposes of the minimum vesting requirements, an employee's years of service completed after the employee has attained age 18.

Break in service rules

The bill provides that, in the case of a nonvested participant, years of service with the employer or employers maintaining the plan before any period of consecutive 1-year breaks in service are required to be taken into account after a break in service unless the number of consecutive 1-year breaks in service equals or ex-

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[16] Sec. 411(b) of the Code.

[17] In addition, the bill changes the maximum age requirement under a plan maintained exclusively for the benefit of employees of certain tax-exempt educational organizations (sec. 410(a)(1)(B)(ii) of the Code) from 30 to 26.

ceeds the greater of (1) 5 years or (2) the aggregate number of years of service before the consecutive 1-year breaks in service. As under present law, if any years of service are not required to be taken into account by reason of a period of breaks in service under this rule, then those years of service are not required to be taken into account under the bill if there is a subsequent break in service. This "rule of parity" is applicable for participation and vesting purposes.

For example, if a nonvested participant with 3 years of service under a plan terminates employment and incurs 4 consecutive 1-year breaks in service, the plan generally is not permitted to disregard the participant's 3 years of service for either participation or vesting purposes upon the participant's resumption of employment with the employer. On the other hand, if the participant incurs 5 consecutive 1-year breaks in service under this example, the plan could disregard the years of service prior to the break in service.

In addition, the bill provides that, in the case of a participant in a defined contribution plan or in a defined benefit pension plan funded solely by insurance contracts, years of service after a break in service are counted for purposes of determining the vested percentage of the participant's accrued benefit derived from employer contributions before the break in service unless the participant incurs at least 5 consecutive 1-year breaks in service. Under the bill, a conforming change is made to the rules relating to the cash out of accrued benefits.

Maternity or paternity leave

Under the bill, for purposes of determining whether a break in service has occurred for participation and vesting purposes, an individual is deemed to have completed hours of service during certain periods of absence from work. This rule applies to an individual who is absent from work (1) by reason of the pregnancy of the individual, (2) by reason of the birth of a child of the individual, (3) by reason of the placement of a child in connection with the adoption of the child by the individual, or (4) for purposes of caring for the child during the period immediately following the birth or placement for adoption.

The committee intends that an individual will qualify for this maternity or paternity leave credit if a child is placed with the individual for a trial period prior to adoption. No credit need be given, however, merely by reason of the placement of a child in a foster home.

During the period of absence, the individual is treated as having completed (1) the number of hours that normally would have been credited but for the absence, or (2) if the normal work hours are unknown, eight hours of service for each normal workday during the leave (whether or not approved). The total number of hours of service required to be treated as completed under the bill is 501 hours.

The hours of service required to be credited under the bill must be credited only (1) in the year in which the absence begins for one of the permitted reasons if the crediting is necessary to prevent a break in service in that year, or (2) in the following year. For example, an individual who completes at least 501 hours during a

year before leaving employment by reason of pregnancy or who is otherwise entitled to credit for up to 501 hours during the year is entitled to credit of up to 501 hours in the next year, because such credit is not needed in the year in which the absence begins.

Under the bill, an individual is not entitled to credit for maternity or paternity leave unless the absence from work is for one of the permitted reasons. For example, suppose that an individual was absent from work on account of a layoff, gave birth to a child two years after the layoff began, and was not recalled to work. Under these circumstances, the individual is not entitled to credit for maternity or paternity leave because the absence from work was not for one of the permitted reasons. On the other hand, if the employer had recalled the individual immediately prior to the birth of the child, the individual would be entitled to credit for maternity or paternity leave.

An employer may require, as a condition of providing credit for the hours required under this rule, that the individual certify to the employer that the leave was taken for the permitted reasons. This certification could be required to include, for example, a statement from a doctor that the leave was taken by reason of the birth of a child of the individual. In addition, the employer may require that the individual supply information relating to the number of normal workdays for which there was an absence. The committee intends that credit will not be denied for failure to supply any required information if the plan administrator has access to the relevant information without regard to whether the participant submits it.

Under the bill, hours credited under these rules for maternity or paternity leave are not required to be taken into account for purposes of determining a participant's year of participation under the benefit accrual rules.

Effective Dates

The service-counting provisions generally are effective for plan years beginning after December 31, 1984. In the case of a plan maintained pursuant to one or more collective bargaining agreements ratified before the date of enactment between employee representatives and one or more employers, the provisions are not effective for plan years beginning before the earlier of (1) the date on which the last of the collective bargaining agreements relating to the plan terminates (determined without regard to any extension agreed to after the date of enactment) or (2) January 1, 1987.

The provisions of the bill relating to the maximum age conditions do not apply retroactively. Thus, for example, if an employee with 3 years of service is age 24 on the effective date, the employee is to immediately become a participant in the pension plan, but need not be given credit, for benefit accrual purposes, for the prior years of service. The provisions of the bill relating to the age at which years of service must be counted for vesting purposes is effective for participants who have at least an hour of service on or after the effective date. Thus, in the above example, the employee would be credited with three years of service for vesting purposes (from age 21) on becoming a participant.

With respect to the maternity or paternity leave provision, if a plan credits hours of service in accordance with the requirements of the provision for plan years beginning after the effective date of the provision for the plan (without regard to whether the plan has been amended), the plan (1) need not be amended to meet the requirements of the provision until the plan is first otherwise amended after the effective date, and (2) does not fail to provide definitely determinable benefits (within the meaning of the tax qualification rules for pension plans under the Internal Revenue Code) merely because the plan provides the required credit for maternity or paternity leave not specified in the plan.

B. Survivor Benefit Requirements (Secs. 103 and 203 of the bill, secs. 205 and 206 of ERISA, and secs. 401 and 417 of the Code)

Present Law

Under present law,[18] if the normal form of benefits under a pension plan is a life annuity or if a participant elects benefits in the form of a life annuity under a plan and the participant is married for the 1-year period ending on the date the annuity payments begin, the benefit is to be paid in the form of a qualified joint and survivor annuity unless the participant elects an annuity in another form.[19] A joint and survivor annuity provides benefits for the joint lives of the participant and another individual and, after the death of either, provides a benefit for the life of the survivor. Under a qualified joint and survivor annuity, benefits are payable for the joint lives of the participant and the participant's spouse and, if the spouse survives the participant, the survivor benefit to the spouse may not be less than one-half of the benefits payable during the joint lives of the couple.

In the case of a participant who is eligible to retire before the normal retirement age under the plan, and who has not retired, the participant is eligible to elect an early survivor annuity benefit. This benefit is not required to be provided, however, unless the participant affirmatively elects benefits in this form. Thus, under present law, if the plan provides that no benefits will be paid with respect to a participant who dies while still employed but after attaining the plan's early retirement age, the plan need not provide a survivor annuity to the participant's spouse unless the participant, prior to death, made an affirmative election with respect to the survivor annuity. Moreover, the plan need not make this survivor annuity option available until the later of the time the employee attains the earliest retirement age under the plan or is within 10 years of normal retirement age (whichever is later).

The employee is to be afforded a reasonable opportunity to elect not to receive a qualified joint and survivor benefit before benefit payments begin. This election is effective without regard to whether the participant's spouse consents to the election. A plan may provide that any election, or revocation of an election, with respect to joint and survivor benefits is not effective if the participant dies

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[18] Sec. 401(a)(11) of the Code.

[19] For example, a participant may elect a benefit in the form of a single life annuity. If a single life annuity is elected, benefit payments generally end with the death of the participant.

within a period of time (not in excess of two years) after making the election or revocation (except in the case of accidental death if the accident that causes death occurs after the election).

The Internal Revenue Service has issued regulations interpreting the joint and survivor annuity rules to provide that a plan need not provide a survivor annuity to a surviving spouse if the spouse was not married to the participant for at least the one-year period before the date of death.[20]

Reasons for Change

The committee believes that present law results in inequitable treatment of participants in pension plans who die before reaching the normal retirement age under the employer's plan. Under the rules of present law, the participant's spouse may be entitled to no survivor benefits under the plan even though the participant had accrued significant vested benefits before death. Therefore, the committee believes that it is appropriate to provide automatic survivor benefits to the spouses of vested participants.

In addition, because the committee believes that a spouse should be involved in making choices with respect to retirement income on which the spouse may also rely, the bill requires spousal consent when a participant elects not to take a survivor benefit.

Explanation of Provision

In general

Under the bill, a pension plan is to provide automatic survivor benefits (1) in the case of a participant who retires under the plan, in the form of a qualified joint and survivor annuity, and (2) in the case of a vested participant who dies before the annuity starting date (the first period for which an amount is received as an annuity (whether by reason of death or disability) under the plan) and who has a surviving spouse, in the form of a qualified preretirement survivor annuity. A vested participant is any participant (whether or not still employed by the employer) who has a nonforfeitable right to any portion of the accrued benefit derived from employer contributions.

The provisions of the bill requiring automatic survivor benefits apply to any pension plan. An exception is provided, however, for a participant under a profit-sharing or stock bonus plan if (1) the plan provides that the nonforfeitable accrued benefits will be paid to the surviving spouse of the participant (or to another beneficiary if the surviving spouse consents or if there is no surviving spouse) if the participant dies, (2) under a plan that offers a life annuity, the participant does not elect payment of benefits in the form of a life annuity, and (3) with respect to the participant, the plan is not a direct or indirect transferee of a plan required to provide automatic survivor benefits. A plan is a transferree of a plan required to provide automatic survivor benefits if the plan (1) receives a direct transfer of assets in connection with a merger, spinoff or conversion of a plan or (2) receives a direct transfer of assets solely

[20] Treas. Reg. sec. 1.401(a)-11(d)(3).

with respect to the participant. Also, a plan is a transferee if it receives amounts from a plan that is a transferee. As under present law, the cost of survivor benefit coverage may be imposed on the participant or beneficiary.

Under the bill, an exception to the application of the rules relating to joint and survivor benefits is provided in the case of certain employee stock ownership plans (ESOPs) for the portion of an employee's accrued benefit that is subject to the requirements of section 409(h) of the Code. This exception applies only if the requirements applicable to profit-sharing and stock bonus plans are also met.

Qualified joint and survivor annuity and qualified preretirement survivor annuity

Under the bill, a qualified joint and survivor annuity is an annuity for the life of the participant with a survivor annuity for the life of the spouse that is not less than 50 percent (and not greater than 100 percent) of the amount that is (1) payable during the joint lives of the participant and the spouse, and (2) the actuarial equivalent of a single life annuity for the life of the participant. A qualified joint and survivor annuity also includes an annuity having the effect of a qualified joint and survivor annuity, which is defined as a benefit at least the actuarial equivalent of the normal form of life annuity or, if greater, any optional form of life annuity. Equivalence may be determined on the basis of consistently applied reasonable actuarial factors if such determination does not result in discrimination in favor of employees who are officers, shareholders, or highly compensated.

The bill defines a qualified preretirement survivor annuity as an annuity for the life of the surviving spouse of the participant. The amount of the payments under a qualified preretirement survivor annuity is not to be less than the payments that would have been made under the qualified joint and survivor annuity if (1) in the case of a participant who dies after attaining the earliest retirement age under the plan, the participant had retired with an immediate qualified joint and survivor annuity on the day before the participant's death, and (2) in the case of a participant who dies on or before the earliest retirement age under the plan, the participant had separated from service on the date of death, survived until the earliest retirement age, and retired at that time with a qualified joint and survivor annuity. In the case of a defined contribution plan, the payments under a qualified preretirement survivor annuity are not to be less than the payments under a single life annuity, the present value of which is at least equal to 50 percent of the participant's account balance on the date of death. Under the bill, the plan is not to prohibit the commencement of the qualified preretirement survivor annuity to the surviving spouse later than the month in which the participant would have reached the earliest retirement age under the plan. If the surviving spouse wishes to delay commencement of benefit payments until a later date and the present value of the benefit is more than $3,500 at the earliest retirement date, then the plan cannot require that benefit payments commence at the participant's earliest retirement

age. Of course, the incidental benefit rule of present law is required to be satisfied with respect to the preretirement survivor benefit.

Election and notice procedures

Under the bill, a participant is to be given the opportunity to waive the qualified joint and survivor annuity and qualified preretirement survivor annuity during the applicable election period. In addition, the participant is permitted to revoke any waiver during the applicable election period. The bill does not limit the number of times a participant may waive a survivor benefit or revoke a waiver.

The bill provides that the consent of a participant's spouse is required for an election to decline the qualified joint and survivor annuity and the qualified preretirement survivor annuity. This consent is to be given in writing at the time of the participant's election, and the consent is to acknowledge the effect of the election. A consent is not valid unless it is witnessed by a plan representative or a notary public. Any consent obtained is effective only with respect to the spouse who signs it.

The requirement that the consent of the spouse be obtained may be waived if it is established to the satisfaction of a plan representative that the consent required cannot be obtained because there is no spouse, because the spouse cannot be located, or because of other circumstances that the Secretary of the Treasury prescribes by regulation.

If the plan administrator acts in accordance with the fiduciary standards of ERISA in securing spousal consent or in accepting the representations of the participant that the spouse's consent cannot be obtained, then the plan will not be liable for payments to the surviving spouse. For example, if the plan administrator receives a notarized spousal consent, valid on its face, which the administrator has no reason to believe is invalid, the plan would certainly be allowed to rely on the consent even if it is, in fact, invalid. In addition, if a third-party payor relies on a consent obtained or determination made by the plan administrator who acts in accordance with the fiduciary standards, or if a third party payor acting in accordance with such standards (whether or not the payor is a plan fiduciary under ERISA) establishes that consent cannot be obtained, then the payor will be relieved of any liability for payments to the surviving spouse.

As under present law, the plan is required to provide to the participant, within a reasonable period of time before the annuity starting date, a written explanation of (1) the terms and conditions of the qualified joint and survivor annuity, (2) the participant's right to make, and the effect of, an election to waive the qualified joint and survivor annuity, (3) the rights of the participant's spouse, and (4) the right to revoke an election and the effect of such a revocation. In addition, the committee intends that plans will provide to participants notification of their rights to decline a qualified preretirement survivor annuity period before the applicable election period. This notice is to be provided within the period beginning on the first day of the plan year in which the participant attains age 32 and ending with the close of the plan year in which the participant attains age 35. This notice is to be comparable to

the notice required with respect to the qualified joint and survivor annuity. Of course, the preretirement survivor benefit coverage may become automatic prior to the time that the participant is entitled to decline such coverage.

Under the bill, a plan is not required to provide notice of the right to waive the qualified joint and survivor annuity or the qualified preretirement survivor annuity if the plan fully subsidizes the cost of the benefit. A plan fully subsidizes the costs of a benefit only if the failure to waive the benefit by a plan participant does not result in either (1) a decrease in any plan benefits with respect to the participant, or (2) in increased plan contributions by the participant. A plan that provides for no employee contributions and does not require employee contributions if the participant does not waive any survivor benefits is treated as not requiring increased plan contributions by the participant. A plan may fully subsidize the cost of the qualified joint and survivor annuity, the qualified preretirement survivor annuity, or both.

The bill defines the applicable election period to mean (1) in the case of a qualified joint and survivor annuity, a period of time not exceeding 90 days before the annuity starting date or (2) in the case of a qualified preretirement survivor annuity, a period beginning on the first day of the plan year in which the participant attains age 35 and ending on the date of the participant's death. If a participant separates from service, the applicable election period begins on that date with respect to benefits accrued before the separation from service. For example, if a participant who is age 30 separates from service with vested, accrued benefits of $4,000, the participant is permitted to waive the qualified preretirement survivor annuity with respect to the benefits of $4,000 at the time of separation from service. If the participant returns to service at age 32, the applicable election period with respect to benefits accrued after the participant returns does not begin until the first day of the plan year in which the participant attains age 35. Thus, the participant will have automatic survivor coverage during the period from age 32 to 35 with respect to the vested benefits accrued during that period, without regard to whether the participant waived the coverage with respect to the pre-separation accrued benefits. At age 35, the participant may waive any preretirement survivor annuity coverage. Of course, a waiver made by a participant or by a participant and spouse is not valid with respect to a future spouse.

Special rules

The bill provides that a qualified joint and survivor annuity is not required to be provided by a plan unless the participant and spouse have been married throughout the one-year period ending on the earlier of (1) the participant's annuity starting date (the first day of the first period for which an amount is received as an annuity (whether by reason of retirement or disability)), or (2) the date of the participant's death. If a participant dies after the annuity starting date, the spouse to whom the participant was married during the one-year period ending on the annuity starting date is entitled to the survivor annuity under the plan whether or not the participant and spouse are married on the date of the participant's

death. This rule does not apply, however, if a qualified domestic relations order (see C. below) otherwise provides for the division or payment of the participant's retirement benefits. For example, a qualified domestic relations order could provide that the former spouse is not entitled to any survivor benefits under the plan.

Under the bill, an exception to the one-year marriage requirement is provided if a participant marries within one year before the annuity starting date and the participant has been married to that spouse for at least one year ending on the date of the participant's death. The committee recognizes that this exception may create administrative burdens for a plan in cases in which the participant has not been married for one year before the payment of benefits commence. The committee intends that the plan may require a participant to notify the plan when the participant has been married for one year so that the plan administrator may alter the form of benefit payments to reflect the qualified joint and survivor annuity if the participant and spouse do not waive it.

If a former spouse of a participant is entitled to receive a portion of the participant's benefit under a qualified domestic relations order, the qualified joint and survivor annuity and qualified preretirement survivor annuity requirements do not apply unless they are consistent with the order. A plan is not required to provide a qualified joint and survivor annuity or a qualified preretirement survivor annuity to the spouse of a participant's former spouse.

The bill provides that a plan may immediately distribute the present value of the benefit under either the qualified joint and survivor annuity or the qualified preretirement survivor annuity if the present value of the benefit does not exceed $3,500. No distribution may be made after the annuity starting date unless the participant and the participant's spouse (or the surviving spouse of the participant) consent in writing to the distribution.

In addition, under the bill, if the present value of the benefit under the qualified joint and survivor annuity or the qualified preretirement survivor annuity exceeds $3,500, the participant and spouse (or the surviving spouse if the participant has died) must consent in writing before the plan can immediately distribute the present value. For purposes of calculating the present value of a benefit as of the date of the distribution, the plan is required to use an interest rate no greater than the rate used by the Pension Benefit Guaranty Corporation (PBGC) in valuing a lump sum distribution upon plan termination. The committee intends that the PBGC rate in effect at the beginning of a plan year may be used throughout the plan year if the plan so provides.

The bill repeals the two-year nonaccidental death rule of present law. Thus, a plan may not provide that any election or revocation of an election does not take effect if (1) the participant dies within a period not in excess of two years beginning on the date of the election or revocation, and (2) the death of the participant is not due to an accident that occurred after the election or revocation.

Consultation with the Secretary of Labor

Under the bill, the Secretary of the Treasury is required to consult with the Secretary of Labor in prescribing regulations under these provisions.

Effective Dates

The qualified joint and survivor annuity and qualified preretirement survivor annuity provisions are effective for plan years beginning after December 31, 1984. In the case of a plan maintained pursuant to one or more collective bargaining agreements ratified by the date of enactment between employee representatives and one or more employers, the provisions are not effective for plan years beginning before the earlier of (1) the date on which the last of the collective bargaining agreements relating to the plan terminates (determined without regard to any extension agreed to after the date of enactment) or (2) January 1, 1987. The spousal consent provision is effective for elections (or revocations of elections) made on or after January 1, 1985.

The qualified joint and survivor and preretirement survivor annuity provisions apply to any participant who performs at least one hour of service under the plan on or after the date of enactment. In addition, a qualified preretirement survivor annuity must be provided (unless another form of benefit is elected) in the case of any participant who (1) performs at least one hour of service under the plan after the date of enactment, (2) dies before the annuity starting date, and (3) dies between the date of enactment and the effective date.

The bill provides a special transition rule for participants who separated from service before the date of enactment and whose benefits are not in pay status as of the date of enactment. This special transition rule only applies in the case of a plan (or successor plan) that is in existence at any time on or after the date of enactment. Under the bill, if (1) such participant completed at least 1 hour of service under the plan after September 1, 1974, (2) separated from service before the first day of the first plan year beginning on or after January 1, 1976, and (3) the plan is required to provide a qualified joint and survivor annuity, then the participant is to be provided the right to elect to receive benefits in the form of a qualified joint and survivor annuity (as defined by ERISA and the Code before the date of enactment of the bill). For example, an election or revocation can be made by the participant without the consent of the participant's spouse because the Code did not require the consent of the participant's spouse.

The bill also provides a special transition rule for participants who separated from service before the date of enactment but after December 31, 1975, and whose benefits are not in pay status as of the date of enactment. This special transition rule only applies in the case of a plan (or a successor plan) that is in existence at any time on or after the date of enactment. Under the bill, if such participant (1) completes at least 1 hour of service in the first plan year beginning after December 31, 1975, (2) has completed at least 10 years of service under the plan, (3) has a nonforfeitable right to all or any portion of the accrued benefit under the plan derived from employer contributions, and (4) did not complete at least 1 hour of service after the date of enactment of the bill, then the participant may elect a qualified preretirement survivor annuity as provided by the bill. The bill provides that the election may be made by a participant after the date of enactment of the bill and

before the earlier of the participant's annuity starting date and the date of the participant's death.

Under the special transition rules of the bill for qualified joint and survivor annunities and qualified preretirement survivor annuities, a plan is not to be required to provide a qualified joint and survivor annuity or a qualified preretirement survivor annuity with respect to a participant unless the plan has received the participant's election of such a benefit. The bill provides that a notice of the right to make such an election is to be provided by the plan in such manner and at such time (or times) as the Secretary of the Treasury may prescribe. The committee intends that a plan will not be treated as having failed to give adequate notice if notice is mailed to the last known address of a participant with the first summary annual report sent after the effective date. In addition, the committee intends that plans are to provide notice after the effective date of the right to elect a qualified joint and survivor annuity at the time a participant applies for benefit payments. The bill provides a penalty for failure to provide the notice. In addition, the bill directs the Secretary of Labor to provide public service announcements informing participants of these transition features.

Under the bill, of course, the benefits provided with respect to a participant who has elected a qualified joint and survivor benefit or a qualified preretirement survivor annuity under either of the transition rules may be actuarially reduced to reflect the cost of the survivor protection.

C. Assignment or Alienation of Benefits in Divorce, Etc., Distributions (Secs. 104 and 204 of the bill, sec. 206 of ERISA, and secs. 401 and 414 of the Code)

Present Law

Generally, under present law, benefits under a pension, profit-sharing, or stock bonus plan (pension plan) are subject to prohibitions against assignment or alienation (spendthrift provisions.) Under present law,[21] certain provisions of ERISA supersede (preempt) State laws relating to pension, etc., plans. A plan that does not include these required spendthrift provisions is not a qualified plan under the Code, and State law permitting such an assignment or alienation is generally preempted by ERISA.

Several cases have arisen in which courts have been required to determine whether the ERISA preemption and spendthrift provisions apply to family support obligations (*e.g.*, alimony, separate maintenance, and child support obligations). In some of these cases, the courts have held that ERISA was not intended to preempt State domestic relations law permitting the attachment of vested benefits for the purpose of meeting these obligations.[22] Some courts have held that the ERISA preemption provision does not prevent application of State law permitting attachment of nonvested benefits for the purpose of meeting family support obligations.[23]

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[21] Sec. 514 of ERISA.

[22] *See, e.g., American Telephone and Telegraph Co. v. Merry*, 592 F.2d 118 (2d Cir. 1979); *Cody v. Riecker*, 594 F.2d 314 (2d Cir. 1979).

[23] *See, e.g., Weir v. Weir*, 415 A.2d 638 (1980); *Kikkert v. Kikkert*, 427 A.2d 76 (1981).

There is a divergence of opinion among the courts as to whether ERISA preempts State community property laws insofar as they relate to the rights of a married couple to benefits under a pension, etc., plan.[24]

The IRS has ruled that the spendthrift provisions are not violated when a plan trustee complies with a court order requiring the distribution of benefits of a participant in pay status to the participant's spouse or children in order to meet the participant's alimony or child support obligations.[25] The IRS has not taken any position with respect to this issue in cases in which the participant's benefits are not in pay status.

Reasons for Change

The committee believes that the spendthrift rules should be clarified by creating a limited exception that permits benefits under a pension, etc., plan to be divided under certain circumstances. In order to provide rational rules for plan administrators, the committee believes it is necessary to establish guidelines for determining whether the exception to the spendthrift rules applies. In addition, the committee believes that conforming changes to the ERISA preemption provision are necessary to ensure that only those orders that are excepted from the spendthrift provisions are not preempted by ERISA.

Explanation of Provision

In general

The bill clarifies the spendthrift provisions by providing new rules for the treatment of certain domestic relations orders. In addition, the bill creates an exception to the ERISA preemption provision with respect to these orders. The bill also provides procedures to be followed by a plan administrator (including the Pension Benefit Guaranty Corporation (PBGC)) and an alternate payee (a child, spouse, former spouse, or other dependent of a participant) with respect to domestic relations orders.

Under the bill, if a domestic relations order requires the distribution of all or a part of a participant's benefits under a qualified plan to an alternate payee, then the creation, recognition, or assignment of the alternate payee's right to the benefits is not considered an assignment or alienation of benefits under the plan if and only if the order is a qualified domestic relations order. Because rights created, recognized, or assigned by a qualified domestic relations order, and benefit payments pursuant to such an order, are specifically permitted under the bill, State law providing for these rights and payments under a qualified domestic relations order will continue to be exempt from Federal preemption under ERISA.

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[24] In *Stone v. Stone*, 633 F.2d 740 (9th Cir. 1980), the court held that ERISA was not intended to preempt community property laws and that a court order requiring a division of retirement benefits did not violate the anti-assignment provisions. In *Francis v. United Technology Corp.* 458 F.Supp. 84 (N.D. Cal. 1978), however, the court held that ERISA's preemption provision prevents the application of State community property law permitting attachment of plan benefits for family support purposes.

[25] Rev. Rul. 80-27, 1980-1 C.B. 8.

Qualified domestic relations order

Under the bill, the term "qualified domestic relations order" means a domestic relations order that (1) creates or recognizes the existence of an alternate payee's right to, or assigns to an alternate payee the right to, receive all or a portion of the benefits payable with respect to a participant under a pension plan, and (2) meets certain other requirements. A domestic relations order is any judgment, decree, or order (including approval of a property settlement agreement) that relates to the provision of child support, alimony payments, or marital property rights to a spouse, former spouse, child, or other dependent of the participant, and is made pursuant to a State domestic relations law (including community property law). Under the bill, an alternate payee includes any spouse, former spouse, child, or other dependent of a participant who is recognized by a qualified domestic relations order as having a right to receive all, or a portion of, the benefits payable under a plan with respect to the participant.

To be a qualified order, a domestic relations order must clearly specify (1) the name and last known mailing address (if available) of the participant and the name and mailing address of each alternate payee to which the order relates, (2) the amount or percentage of the participant's benefits to be paid to an alternate payee or the manner in which the amount is to be determined, and (3) the number of payments or period for which payments are required. The committee intends that an order will not be treated as failing to be a qualified order merely because the order does not specify the current mailing address of the participant and alternate payee if the plan administrator has reason to know that address independently of the order. For example, if the plan administrator is aware that the alternate payee is also a participant under the plan and the plan records include a current address for each participant, the plan administrator may not treat the order as failing to qualify.

The committee intends that an order that is qualified is to remain qualified with respect to a successor plan of the same employer or a plan of a successor employer (within the meaning of sec. 414(a)).

A domestic relations order is not a qualified order if it (1) requires a plan to provide any type or form of benefit, or any option, not otherwise provided under the plan, (2) requires the plan to provide increased benefits, or (3) requires payment of benefits to an alternate payee that are required to be paid to another alternate payee under a previously existing qualified domestic relations order. An order does not require a plan to provide increased benefits if the order does not provide for the payment of benefits in excess of the benefits to which the participant would be entitled in the absence of the order.

The bill provides that a domestic relations order is not treated as failing the requirements for a qualified domestic relations order merely because the order provides that payments must begin to the alternate payee on or after the date on which the participant attains the earliest retirement age under the plan whether or not the participant actually retires on that date. If the participant dies

before that date, the alternate payee is entitled to benefits only if the qualified domestic relations order requires survivor benefits to be paid. In the case of an order providing for the payment of benefits after the earliest retirement age, the payments to the alternate payee at that time are computed as if the participant had retired on the date on which benefit payments commence under the order.

When payments are made to an alternate payee before the participant retires, the payments are computed by taking into account only benefits actually accrued and not taking into account any employer subsidy for early retirement. The amount to be paid to the alternate payee is to be calculated by using the participant's normal retirement benefit accrued as of the date payout begins and by actuarially reducing such benefit based on the interest rate specified in the plan or 5 percent, if the plan does not specify an interest rate. A plan providing only normal and subsidized early retirement benefits would not specify a rate for determining actuarially equivalent, unsubsidized benefits.

If an alternate payee begins to receive benefits under the order and the participant subsequently retires with subsidized early retirement benefits, the order may specify that the amount payable to the alternate payee is to be recalculated so that the alternate payee also receives a share of the subsidized benefit to which the participant is entitled. The payment of early retirement benefits with respect to a participant who has not yet retired or the increase in benefits payable to the alternate payee after the recalculation is not to be considered to violate the prohibition against a qualified domestic relations order providing for increased benefits.

The payments to the alternate payee after the earliest retirement date may be paid in any form permitted under the plan (other than a joint and survivor annuity with respect to the alternate payee and the alternate payee's spouse). In the case of a defined contribution plan, the earliest retirement date is the date on which the participant attains an age that is 10 years before the normal retirement age.

Under the bill, a plan is not treated as failing to satisfy the requirements of section 401(a), 409(d), or 401(k) of the Internal Revenue Code that prohibit payment of benefits prior to termination of employment solely because the plan makes payments to the alternate payee in accordance with a qualified domestic relations order.

Under the bill, an alternate payee is treated as a beneficiary for all purposes under the plan. In no event, however, will more than one PBGC premium be collected with respect to the participant's benefits (determined as if a qualified domestic relations order had not been issued) even though such benefits, subject to the usual limits, may be guaranteed by the PSGC.

Determination by plan administrator

Under the bill, the administrator of a plan that receives a domestic relations order is required to notify promptly the participant and any other alternate payee of receipt of the order and the plan's procedures for determining whether the order is qualified. In addition, within a reasonable period after receipt of the order, the plan administrator is to determine whether the order is qualified and notify the participant and alternate payee of the determination.

The notices required under these rules are to be sent to the addresses specified in the order or, if the order fails to specify an address, to the last address of the participant or alternate payee known to the plan administrator.

The bill authorizes the Secretary of Labor to prescribe regulations defining the reasonable period during which the plan administrator is to determine whether an order is qualified. In addition, the bill provides that plans are to establish reasonable procedures to determine whether domestic relations orders are qualified and to administer distributions under qualified orders. Ordinarily, a plan need not be amended to implement the domestic relations provisions of the bill.

Deferral of benefit payments

During any period in which the issue of whether a domestic relations order is a qualified order is being determined (by the plan administrator, by a court of competent jurisdiction, or otherwise), the plan administrator is to defer the payment of any benefits in dispute. These deferred benefits are segregated either in a separate account in the plan or in an escrow account. In the case of a defined benefit plan, the amounts are to be placed in an escrow account. Of course, segregation is not required for amounts that would not otherwise be paid during the period of the dispute.

If the order is determined to be a qualified domestic relations order within 18 months after the deferral of benefits, the plan administrator is to pay the segregated amounts (plus interest) to the persons entitled to receive them. If the plan administrator determines that the order is not a qualified order or, after the 18-month period has expired, has not resolved the issue of whether the order is qualified, the segregated amounts are paid to the person or persons who would have received the amounts if the order had not been issued.

Any determination that an order is qualified after expiration of the 18-month period is to be applied prospectively. Thus, if the plan administrator determines that the order is qualified after the 18-month period, the plan is not liable for payments to the alternate payee for the period before the order is determined to be qualified.

Of course, the provisions of the bill do not affect any cause of action that an alternate payee may have against the participant. For example, if an order is determined to be qualified after the 18-month period, the alternate payee may have a cause of action under State law against the participant for amounts paid to the participant that should have been paid to the alternate payee.

During any period in which the alternate payee cannot be located, the plan is not permitted to provide for the forfeiture of the amounts that would have been paid unless the plan provides for full reinstatement when the alternate payee is located.

Consultation with the Secretary of the Treasury

Under the bill, the Secretary of Labor is required to consult with the Secretary of the Treasury in prescribing regulations under these provisions.

Tax treatment of divorce distributions

The bill provides rules for determining the tax treatment of benefits subject to a qualified domestic relations order. Under the bill, for purposes of determining the taxability of benefits, the alternate payee is treated as a distributee with respect to payments received from or under a plan.

Under the bill, net employee contributions (together with other amounts treated as the participant's investment in the contract) are apportioned between the participant and the alternate payee under regulations prescribed by the Secretary of the Treasury. The apportionment is to be made pro rata, on the basis of the present value of all benefits of the participant under the plan and the present value of all benefits of the alternate payee under the plan (as alternate payee with respect to the participant under a qualified domestic relations order).

Payments to an alternate payee before the participant attains age 59½ are not subject to the 10-percent additional income tax that would otherwise apply under certain circumstances if the participant received the amounts.

The bill provides that the interest of the alternate payee is not taken into account in determining whether a distribution to the participant is a lump sum distribution. Under the bill, benefits distributed to an alternate payee under a qualified domestic relations order can be rolled over, tax-free, to an individual retirement account or to an individual retirement annuity. The usual income tax rules apply to benefits not rolled over. The special rules for lump sum distributions from qualified plans will not apply to benefits distributed to an alternate payee.

Effective Dates

The provisions of the bill relating to assignments in divorce, etc., proceedings generally apply on January 1, 1985. If a domestic relations order was received by a plan before the date of enactment, however, the plan administrator is to treat the order as a qualified domestic relations order to the extent payments are being made pursuant to the order. In addition, the plan administrator may treat any other order entered before the effective date as a qualified order. The committee encourages plan administrators to treat an existing order as qualified to the extent it is consistent with the provisions of the bill. Of course, if the plan administrator does not treat an order as qualified, the alternate payee may amend the order to satisfy the requirements for a qualified order.

D. Cash Out of Certain Accrued Benefits (Secs. 105 and 205 of the bill, sec. 203 of ERISA, and sec. 411 of the Code)

Present Law

Under present law,[26] in the case of an employee whose plan participation terminates, a pension, profit-sharing, or stock bonus plan (pension plan) may involuntarily "cash out" the benefit (*i.e.*, pay out the balance to the credit of a plan participant without the par-

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[26] Sec. 411(a)(7)(B) of the Code.

ticipant's consent) if the present value of the benefit does not exceed $1,750. If a benefit is cashed-out under this rule and the participant subsequently returns to employment covered by the plan, then service taken into account in computing benefits payable under the plan after the return need not include service with respect to which benefits were cashed out unless the employee "buys back" the benefit.

Generally, a cash-out distribution from a qualified plan can be rolled over, tax-free, to an IRA or to another qualified plan.

Under present law, the prohibition on involuntary cash-outs of amounts in excess of $1,750 does not apply to the benefits that may be payable to a surviving or former spouse of the participant.

Reasons for Change

The committee believes that the limit on involuntary cash-outs should be raised to $3,500 in recognition of the effects of inflation on the value of small benefits payable under a pension plan.

Explanation of Provisions

The bill provides that, if the present value of an accrued benefit exceeds $3,500, then the benefit is not to be considered nonforfeitable if the plan provides that the present value of the benefit can be immediately distributed without the consent of the participant (and, if applicable, the participant's spouse). Under the bill, the interest rate to be used in determining whether the present value of a benefit exceeds $3,500 is not to be greater than the interest rate that would be used (as of the date of the distribution) by the Pension Benefit Guaranty Corporation (PBGC) for purposes of determining the present value of a lump sum distribution upon termination of the plan. The committee intends that the PBGC rate in effect at the beginning of a plan year may be used throughout the plan year if the plan so provides.

Effective Date

The cash-out provision generally is effective for plan years beginning after December 31, 1984. In the case of a plan maintained pursuant to one or more collective bargaining agreements ratified by the date of enactment between employee representatives and one or more employers, the provision is not effective for plan years beginning before the earlier of (1) the date on which the last of the collective bargaining agreements relating to the plan terminates (determined without regard to any extension agreed to after the date of enactment) or (2) January 1, 1987.

E. Notice of Forfeitability of Benefits (Secs. 106 and 206 of the bill, sec. 105 of ERISA, and sec. 6057 of the Code)

Present Law

Under present law, the administrator of a pension, profit-sharing, or stock bonus plan (pension plan) is required to furnish to a plan participant a statement indicating the participant's total accrued benefits and nonforfeitable accrued benefits if the partici-

pant requests such a statement. A participant is not entitled to more than one statement during any 12-month period. In addition, present law requires a plan administrator to furnish a statement to each plan participant who (1) separates from service during a plan year, (2) is entitled to a vested deferred benefit under the plan, and (3) did not receive retirement benefits under the plan during the year. This statement must contain specified information relating to the benefit.

Reasons for Change

The committee believes that a participant who receives a statement of accrued benefits as required under present law should be informed of any benefits that may be forfeited if the participant dies prior to a particular date so that participants may make financial arrangements for the retirement security of their spouses.

Explanation of Provision

Under the bill, any statement provided to a plan participant of total accrued benefits and nonforfeitable accrued benefits, or any statement provided to a separated plan participant who has a vested deferred benefit, must include a notice to the participant that certain benefits may be forfeited if the participant dies before a particular date. The notice that certain benefits may be forfeited if a participant dies before a particular date need not include the amount of the benefits that are forfeitable.

Effective Date

The provision of the bill requiring notice of forfeitability of benefits is effective for plan years beginning after December 31, 1984. In the case of a plan maintained pursuant to one or more collective bargaining agreements ratified by the date of enactment between employee representatives and one or more employers, the provision is not effective for plan years beginning before the earlier of (1) the date on which the last of the collective bargaining agreements relating to the plan terminates (determined without regard to any extension agreed to after the date of enactment) or (2) January 1, 1987.

F. Notice of Rollover Treatment (Sec. 207 of the bill and secs. 402 and 6652 of the Code)

Present Law

Under present law, an employee's benefits from or under a qualified plan generally are includible in income when the benefits are distributed. If the balance to the credit of an employee is paid to the employee or to the surviving spouse of the employee as a qualifying rollover distribution, all or any portion of the distribution may be rolled over, within 60 days of the date of the distribution, to another qualified plan or an IRA. If a rollover is made, tax is deferred on the portion of the distribution rolled over. Similar rules apply to qualifying rollover distributions from or under a tax-sheltered annuity contract. If a rollover is not made, the partici-

pant or beneficiary may be eligible for 10-year income averaging (or long-term capital gains treatment) with respect to the distribution.

Present law does not require a plan administrator to notify a recipient of a qualifying rollover distribution of the time for making a rollover to another qualified pension plan or an IRA or the consequences of rolling over the distribution. Also, no notice is required to be provided relating to eligibility for 10-year income averaging.

Reasons for Change

The committee is concerned that participants in qualified plans and the surviving or former spouses of participants often fail to make rollovers of qualifying rollover distributions because they do not understand the consequences of making such a rollover. In addition, the committee is aware that many individuals have failed to make permissible rollovers because they do not make the rollover within the required time period. The committee believes that the plan administrator can, without significant administrative burden, provide this information and information relating to 10-year income averaging to the person receiving the distribution.

Explanation of Provision

Under the bill, when the administrator of a qualified plan makes a qualifying rollover distribution, the administrator is to provide notice to the recipient that (1) the distribution will not be taxed currently to the extent transferred to another qualified pension plan or an IRA, and (2) the transfer must be made within 60 days of receipt in order to qualify for this tax-free rollover treatment. In the case of a series of distributions that may constitute a lump sum distribution, the committee intends that this notice will explain that the 60-day period does not begin to run until the last distribution is made. In addition, this notice is to provide a written explanation of the 10-year income averaging and capital gains provisions if applicable.

The committee intends that the Secretary of the Treasury will provide an officially approved notice that plan administrators may use to satisfy this notice requirement.

The committee recognizes that, under certain circumstances, it may be difficult for a plan administrator to determine whether a particular distribution is a qualifying rollover distribution. Thus, your committee intends that a plan administrator satisfies the notice requirement if notice is provided with every payment from or under the plan so long as the notice, in addition to satisfying the other requirements, includes a statement describing how a recipient may determine whether the particular distribution is a qualifying rollover distribution.

Failure of the plan administrator to give the required notice of rollover treatment results in imposition of a $10 penalty for each failure up to $5,000 for each calendar year. This penalty does not apply if the failure is shown to be due to reasonable cause and not to willful neglect.

Effective Date

The notice provision generally is effective for plan years beginning after December 31, 1984. In the case of a plan maintained pursuant to one or more collective bargaining agreements ratified before the date of enactment between employee representatives and one or more employers, the provision is not effective for plan years beginning before the earlier of (1) the date on which the last of the collective bargaining agreements relating to the plan terminates (without regard to any extension agreed to after the date of enactment) or (2) January 1, 1987.

G. Reduction of Accrued Benefits (Sec. 301 of the bill)

Present Law

Under present law, a pension plan is not a qualified plan unless all benefits provided by the plan are definitely determinable. The Internal Revenue Service takes the position that a defined benefit pension plan is not a qualified plan unless, whenever the amount of any benefit is to be determined on the basis of actuarial assumptions, such assumptions are specified in the plan in a manner that precludes employer discretion.[27]

In addition, present law provides that a qualified plan generally may not be amended in a manner that decreases the benefits of any participant accrued prior to the amendment.[28] An exception to this rule is provided for certain retroactive plan amendments. Under an IRS ruling, for purposes of determining whether a participant's accrued benefit is decreased, all of the provisions of the plan affecting directly or indirectly the accrued benefit are taken into account.[29] Also, the reduction of a benefit or elimination of an option is prohibited under a qualified plan if it results in discrimination in favor of employees who are officers, shareholders, or highly compensated.

Reasons for Change

The committee believes that the protection of accrued benefits, which are essentially retirement benefits, against reduction by plan amendments is an essential safeguard for plan participants and their beneficiaries. The committee also believes that valuable rights of participants should not be lost through the elimination of benefit options because options of equal actuarial value may not be of equal value to people whose particular circumstances are not taken into account in determining actuarial equivalence.

Explanation of Provisions

In general

Under the bill, as under present law, the accrued benefit of a participant is not to be decreased by an amendment of a plan.[30]

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[27] Rev. Rul. 79-90, 1979-1C.B. 155.
[28] Sec. 411(d)(6).
[29] Rev. Rul. 81-12, 1981-1C.B. 228.
[30] Other than an amendment described in section 412(c)(8) of the Code or section 4281 of ERISA.

The bill clarifies the scope of the prohibition against such decreases. The committee intends that no inference is to be made on the basis of this clarification as to the scope of the prohibition before the effective date of the provision.

The bill provides that an amendment of a qualified plan is to be treated as reducing accrued benefits if, with respect to benefits accrued before the amendment is adopted, the amendment has the effect of either (1) eliminating or reducing an early retirement benefit or a retirement-type subsidy, or (2) except as provided by Treasury regulations, eliminating an optional form of benefit. The bill does not, however, prevent changes with respect to future benefit accruals.

The bill generally protects the accrual of benefits with respect to participants who have met the requirements for a benefit as of the time a plan is amended and participants who subsequently meet the preamendment requirements. The bill does not, however, prevent the reduction of a subsidy in the case of a participant who, at the time of separation from service (whether before or after the plan amendment), has not met the preamendment requirements. The provision does not change any rules under which accrued benefits become vested.

Accordingly, the bill makes it clear that the prohibition against reduction of a benefit subsidy (the excess of the value of a benefit over the actuarial equivalent of the normal retirement benefit) applies to a participant only if the participant meets the conditions imposed by the plan on the availability of the subsidy. If the protection is afforded, an employee's accrued benefit is not to be less than the protected level or the accrued benefit determined under the plan without regard to the protection, whichever is greater. For example, if a plan is amended to eliminate a subsidized early retirement benefit for employees who have completed 30 years of service, then the plan would not be required to provide the subsidy to an employee who never completes 30 years of service and it would not be required to provide benefis to such an employee before the normal retirement age. On the other hand, if the employee completes 30 years of service, then the employee's accrued benefit is not to be less than the protected level or the accrued benefit determined without regard to the protection, whichever is greater. Accordingly, if a benefit subsidy is provided, for example, only for employees who retire during a "window period", the provision would not require that benefits of an employee who does not retire during the window period include the window benefit. Also, the provision would not affect the application of any other provision of the Code, such as section 401(a)(1) or 411(b)(1)(G).

For example, consider a plan that provides an annual benefit of 1 percent of average pay per year of service at normal retirement age under the plan (age 65). The plan provides an early retirement benefit to a participant who has attained age 55. This early retirement benefit is actuarially reduced to 50 percent of the benefit payable to the participant at age 65. In the case of a participant who attains age 55 and who has completed 30 years of service, the amount of the annual benefit payable beginning at age 55 is not actuarially reduced under the plan.

Under the bill, if the plan is amended on January 1, 1985 (effective on that date), to require a full actuarial reduction of early retirement benefits in all cases, then the full actuarial reduction could be made for any participant who severs employment before attaining age 55 and completing 30 years of service. Under the bill, however, if a participant met the age and service requirements for the unreduced early retirement benefit on January 1, 1985, then the plan amendment could not reduce that benefit below the level to which the participant would have been entitled if retirement had occurred immediately before the plan amendment was effective.

Under this plan, if a participant did not meet the plan's requirements for unreduced early retirement benefits on January 1, 1985, but the participant later satisfies those requirements, then the participant's accrued benefit under the plan would be the greater of (1) the accrued benefit as of the date of the plan amendment, without taking the actuarial reduction into account, or (2) the accrued benefit provided by the plan when the benefit becomes payable, after the full actuarial reduction. Accordingly, the participant's accrued benefit will not be reduced by the plan amendment, but it will not be increased by subsequent service or pay raises until the subsequent increase brings the participant's accrued benefit to a level in excess of the accrued benefit as of January 1, 1985.

The following examples illustrate the application of this provision.

Employee A was covered by the plan described above and, on January 1, 1985, was one day short of attaining age 55 and had completed 30 years of service. If A's average pay immediately before the amendment was $10,000, then A's accrued benefit at that time was an annual benefit of $3,000 ($10,000×1 percent×30 years). A 50-percent actuarial reduction would reduce A's benefit payable beginning on January 1, 1985, to $1,500. Under the bill, the plan amendment could not reduce A's accrued benefit below $3,000 if A later attains age 55.

If as of January 1, 1985, employee B was age 50, had completed 25 years of service, and had average pay of $10,000, then the plan amendment could not reduce B's benefit below $2,500 ($10,000×1 percent×25 years). If B's average pay increased at 6 percent annually until age 55, then B's accrued benefit at age 55 under the plan as amended would be $4,016 ($13,382×1 percent×30 years). But for the bill and prior law, the actuarial reduction would reduce B's annual benefit to $2,008. Under the bill, the amendment could not reduce B's benefit payable at age 55 below $2,500.

If as of January 1, 1985, employee C was age 45, had completed 20 years of service, and had average pay of $10,000, and C's pay increased at 6 percent annually until age 55, then C's benefit would not be increased under the bill. C's accrued benefit as of January 1, 1985, was $2,000 ($10,000 × 1 percent × 20), and at age 55 (assuming average pay rises at 6 percent annually to $17,906) C's accrued benefit will be $5,371 ($17,906 × 1 percent × 30 years). The 50-percent actuarial reduction would reduce C's benefit to $2,685. The bill does not affect the result in C's case because the actuarial reduction does not reduce C's benefit below the protected level of $2,000.

Of course, a plan provision that takes effect as a result of a change in the status of the plan from top heavy to non-top heavy would be treated as a plan amendment at the time the specified event occurs. Accordingly, such a provision is not to have the effect of reducing previously accrued benefits.

The bill does not change the rules under which accrued benefits may be reduced with the consent of the Secretary of Labor, in the event of a substantial business hardship (sec. 412(c)(8) of the Code) or the rules permitting a reduction of benefits in the case of certain multiemployer plans (sec. 4281 of ERISA). Also, the committee expects that Treasury regulations will permit participants to elect to reduce accrued benefits in a defined benefit pension plan where those benefits would otherwise exceed the overall limits on contributions and benefits (sec. 415 of the Code) or cause prohibited discrimination under the plan.

Retirement-type subsidy

The bill provides that the term "retirement-type subsidy" is to be defined by Treasury regulations. The committee intends that under these regulations, a subsidy that continues after retirement is generally to be considered a retirement-type subsidy. The committee expects, however, that a qualified disability benefit, a medical benefit, a social security supplement, a death benefit (including life insurance), or a plant shutdown benefit (that does not continue after retirement age) will not be considered a retirement-type subsidy. The committee expects that Treasury regulations will prevent the recharacterization of retirement-type benefits as benefits that are not protected by the provision.

Elimination of optional benefit forms

Under the bill, to the extent provided by Treasury regulations, a benefit option may be eliminated with respect to benefits accrued before the date the amendment is adopted. The committee expects that, for example, the elimination of an option with respect to previously accrued benefits is not to be prohibited by a plan amendment to the extent the elimination of the option is required as a condition of meeting the standards for qualified status of the plan.

The regulations also could permit the elimination of an option if (1) the elimination of the option does not eliminate a valuable right of a participant or beneficiary, and (2) the option is not subsidized or a similar benefit with a comparable subsidy is provided. For example, if a plan provides a joint and full, a joint and ⅔, and a joint and ½ survivor benefit, the elimination of the joint and ⅔ survivor benefit would not eliminate a valuable participant right. The elimination of all joint and survivor options would not be permissible. The committee expects that the regulations will not permit the elimination of a "lump-sum distribution" option because, for a participant or beneficiary with substandard mortality, the elimination of that option could eliminate a valuable right even if a benefit of equal actuarial value (based on standard mortality) is available under the plan. Of course, the right to select an investment option under a defined contribution plan is not an optional benefit form.

Terminated plans

The bill does not provide an exception to the prohibition against reduction of benefits or elimination of benefit options in the case of a terminated plan. Accordingly, a plan is not to be considered to have satisfied all of its liabilities to participants and beneficiaries until it has provided for the payment of contingent liabilities with respect to a participant who, after the date of the termination of a plan, meets the requirements for a subsidized benefit. The committee does not, however, intend that the absence of such an exception is to affect the liability of the Pension Benefit Guaranty Corporation (PBGC) with respect to benefits under terminated plans. The committee intends that the provision is not to be construed as changing the liability of the PBGC for guaranteed benefits. The committee recognizes that there is a potential for abuses with respect to plan terminations under the provision. If abuses of this type develop, further legislation may be necessary in order to resolve these problems, if administrative solutions are inadequate.

Effective Date

Generally, the provision applies to plan amendments made after July 30, 1984. A special effective date is provided with respect to a plan maintained pursuant to one or more collective bargaining agreements between employee representatives and one or more employers. Under the bill, if such agreements are successor agreements to one or more collective bargaining agreements that terminate after July 30, 1984, and before January 1, 1985, then the provision does not apply to plan amendments adopted after July 30, 1984, and before April 1, 1985, pursuant to such agreements. Under the provision, of course, if negotiations are completed by January 1, 1985, with respect to a collective bargaining agreement, then a plan amendment made pursuant to a later reopening of the negotiations would be prohibited if it reduces or eliminates protected benefits.

For example, the provision would prohibit an amendment to a plan (whether or not the plan is maintained pursuant to a collective bargaining agreement) made on April 1, 1985, that has the effect of reducing a protected benefit which was provided by a plan amendment made during 1980. Such an amendment would be prohibited whether or not it was made pursuant to a provision of a collective bargaining agreement relating to the reopening of negotiations.

H. Study by the General Accounting Office (Sec. 304 of the bill)

The bill provides that the General Accounting Office (GAO) is to conduct a detailed study (based on a reliable scientific sample of typical pension, profit-sharing, and stock bonus plans of various designs and sizes) of the effect on women of participation, vesting, benefit accrual, funding, integration, survivorship features, and other relevant plan and Federal pension rules. In connection with this study, the bill provides that GAO is to have access to the records of employers maintaining pension plans and to the records of the plans.

GAO is directed under the bill to consult with the Internal Revenue Service, the Department of Labor, and other interested Federal agencies to prevent the duplication of data compilation or analyses.

The report is required to be transmitted, no later than January 1, 1990, to the House Committee on Ways and Means, the House Committee on Education and Labor, the Senate Committee on Finance, the Senate Committee on Labor and Human Resources, and the Joint Committee on Taxation.

III. BUDGET EFFECTS AND VOTE OF THE COMMITTEE

Budget Effects

In compliance with paragraph 11(a) of Rule XXVI of the Standing Rules of the Senate, the following statement is made relative to the budget effects of H.R. 4280, as reported.

The revenue provisions of the bill involving statutory changes are estimated to reduce fiscal year budget receipts by $42 million in 1985, $67 million in 1986, $83 million in 1987, $90 million in 1988, and $93 million in 1989. The total revenue lost during the first three fiscal years, 1985 through 1987, equals $192 million.

The Treasury Department agrees with this statement.

The table following provides detailed estimates for the tax provisions of the bill for fiscal years 1985–89.

Vote of the Committee

In compliance with paragraph 7(c) of Rule XXVI of the Standing Rules of the Senate, the following statement is made about the vote of the committee on the motion to report the bill, as amended. The bill, H.R. 4280, as amended, was ordered favorably reported unanimously without objection.

ESTIMATED REVENUE EFFECTS OF TAX PROVISIONS OF H.R. 4280, AS REPORTED BY THE COMMITTEE ON FINANCE

FISCAL YEARS, 1985-89

[In millions of dollars]

Provision	1985	1986	1987	1988	1989
A. Crediting periods of service:					
1. Lower maximum participation age in pension plans to 21 years	−34	−59	−75	−82	−85
2. Years of service after age 18 counted for vesting under pension plans	[1]	[1]	[1]	[1]	[1]
3. Rule of parity applied only if break in service exceeds 5 years	[2]	[2]	[2]	[2]	[2]
4. Maternity or paternity leave not treated as break in service	[3]	[3]	[3]	[3]	[3]
B. Joint and survivor annuity and preretirement survivor benefits	[4]	[4]	[4]	[4]	[4]
C. Distributions of benefits upon divorce	[3]	[3]	[3]	[3]	[3]
D. Involuntary cash-outs	[5]	[5]	[5]	[5]	[5]
E. Cutback in accrued benefits					
Total, tax provisions [6]	−42	−67	−83	−90	−93

[1] Loss of less than $10,000,000.
[2] Negligible loss.
[3] Loss of less than $5,000,000.
[4] Gain of less than $5,000,000.
[5] Negligible gain.
[6] For the purpose of arriving at totals, estimates appearing as footnotes are assigned the following values: negligible equals zero; loss of less than $5,000,000 equals −$3,000,000; loss of less than $10,000,000 equals −$5,000,000; gain of less than $5,000,000 equals $3,000,000.

IV. REGULATORY IMPACT OF THE BILL AND OTHER MATTERS TO BE DISCUSSED UNDER SENATE RULES

Regulatory Impact

Pursuant to paragraph 11(b) of Rule XXVI of the Standing Rules of the Senate, the committee makes the following statement concerning the regulatory impact that might be incurred in carrying out the provisions of H.R. 4280, as reported.

Number of individuals and businesses who would be regulated

The bill does not involve new or expanded regulation of individuals or businesses.

Economic impact of regulation on individuals, consumers, and business

The bill provides modifications to the treatment of pension plan rules as they affect spouses, and generally lowers the maximum plan participation age to 21 and the maximum vesting age to 18.

Impact on personal privacy

The bill generally does not relate to the personal privacy of individuals. The bill does create an exception to the ERISA prohibition against the alienation or assignment of benefits for certain court orders relating to child support, alimony or other material property rights.

Determination of the amount of paperwork

The bill will involve some additional paperwork for taxpayers, but the bill generally involves modifications of existing required recordkeeping relating to pension plans.

Other Matters

Consultation with Congressional Budget Office on budget estimates

In accordance with section 403 of the Budget Act, the committee advises that the Director of the Congressional Budget Office has examined the committee's budget estimates of the tax provisions of the bill (as shown in Part III of this report) and agrees with the methodology used and the committee's budget estimates. The Director submitted the following statement.

New budget authority

In compliance with section 308(a)(1) of the Budget Act, and after consultation with the Director of the Congressional Budget Office, the committee states that the changes made to existing law by the bill involve new budget authority.

U.S. CONGRESS,
CONGRESSIONAL BUDGET OFFICE,
Washington, DC, August 1, 1984.

Hon. ROBERT J. DOLE,
Chairman, Committee on Finance,
U.S. Senate, Washington, DC.

DEAR MR. CHAIRMAN: In accordance with Section 403 of the Congressional Budget Act, the Congressional Budget Office has examined H.R. 4280, the Retirement Equity Act of 1984, as ordered reported by the Committee. H.R. 4280 is intended to improve benefit protection and provide for greater equity in private pension plans for workers and their spouses and dependents. The provisions of the bill, as amended by the Committee, address issues related to the crediting of periods of service under qualified pension plans, providing of survivor benefits to the spouses of participants under pension plans, and modifying and clarifying federal tax and labor law rules with respect to certain distributions from qualified pension plans pursuant to state domestic relations orders. In addition, the bill would require the General Accounting Office to prepare a detailed study of the effects on women of the rules relating to pension, profit sharing, and stock bonus plans.

CBO has reviewed and concurs with estimates of the revenue effect of H.R. 4280 prepared by the staff of the Joint Committee on Taxation. The bill would increase tax expenditures and reduce fiscal year revenues by $42 million in 1985, $67 million in 1986, $83 million in 1987, $90 million in 1988, and $93 million in 1989.

Should the committee so desire, we would be pleased to provide further details on this estimate.

With best wishes.

Sincerely,

RUDOLPH G. PENNER.

Tax expenditures

In compliance with section 308(a)(2) of the Budget Act with respect to tax expenditures, and after consultation with the Director of the Congressional Budget Office, the committee states that the changes made to existing law by the bill as amended will involve increased tax expenditures of the amounts of revenue losses for fiscal years 1985–89 shown in the table above (in Part III) of this report.

V. CHANGES IN EXISTING LAW MADE BY THE BILL, AS REPORTED

In the opinion of the committee, it is necessary, in order to expedite the business of the Senate, to dispense with the requirements of paragraph 12 of Rule XXVI of the Standing Rules of the Senate (relating to the showing of changes in existing law made by the provisions of H.R. 4280, as reported by the committee).